



GARP

2016-FRR Exam

Financial Risk and Regulation (FRR) Series Exam

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Question 1. (Single Select)

Which one of the following four statements correctly defines credit risk?

- A: Credit risk is the risk that complements market and liquidity risks.
- B: Credit risk is a form of performance risk in contractual relationship.
- C: Credit risk is the risk arising from execution of a company's strategy.
- D: Credit risk is the risk that summarizes the exposures a company or firm assumes when it attempts to operate within a given field or industry.

Correct Answer: B

Question 2. (Single Select)

Alpha Bank determined that Delta Industrial Machinery Corporation has 2% change of default on a one-year no-payment of USD \$1 million, including interest and principal repayment. The bank charges 3% interest rate spread to firms in the machinery industry, and the risk-free interest rate is 6%. Alpha Bank receives both interest and principal payments once at the end the year. Delta can only default at the end of the year. If Delta defaults, the bank expects to lose 50% of its promised payment.

What may happen to the Delta's initial credit parameter and the value of its loan if the machinery industry experiences adverse structural changes?

- A: Probability of default and loss at default may decrease simultaneously, while duration rises causing the loan value to decrease.
- B: Probability of default and loss at default may decrease simultaneously, while duration falls causing the loan value to decrease.
- C: Probability of default and loss at default may increase simultaneously, while duration rises causing the loan value to decrease.
- D: Probability of default and loss at default may increase simultaneously, while duration falls causing the loan value to decrease.

Correct Answer: C

Question 3. (Single Select)

Alpha Bank determined that Delta Industrial Machinery Corporation has 2% change of default on a one-year no-payment of USD \$1 million, including interest and principal repayment. The bank charges 3% interest rate spread to firms in the machinery industry, and the risk-free interest rate is 6%. Alpha Bank receives both interest and principal payments once at the end the year. Delta can only default at the end of the year. If Delta defaults, the bank expects to lose 50% of its promised payment. Six months after Alpha Bank provides USD \$1 million loan to the Delta Industrial Machinery Corporation, a new competitor enters the machinery industry, causing Delta to adjust its prices and mark down the value of its inventory. Hence, the probability of default increases from 2% to 10% and the loss given default increases from 50% to 75%. If Alpha Bank can reprice the loan, what should the new rate be?

- A: 10%
- B: 13%
- C: 16.5%
- D: 20.5%

Correct Answer: D

Question 4. (Single Select)

Which one of the following four model types would assign an obligor to an obligor class based on the risk characteristics of the borrower at the time the loan was originated and estimate the default probability based on the past default rate of the members of that particular class?

- A: Dynamic models
- B: Causal models
- C: Historical frequency models
- D: Credit rating models

Correct Answer: C

Question 5. (Single Select)

Which one of the following four models is typically used to grade the obligations of small- and medium-size enterprises?

- A: Causal models
- B: Historical frequency models
- C: Credit scoring models
- D: Credit rating models

Correct Answer: C



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